

BUDGET LETTER

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| | | NUMBER: 04-10 |
| SUBJECT: ENCUMBERING AGREEMENTS AND THE LIQUIDATION OF ENCUMBRANCES | | DATE ISSUED: June 16, 2004 |
| REFERENCES: California Code of Regulations, Title 2, Division 2, Chapter 1, Article 2, Section 610; Budget Letters 03-43, 04-01, 04-08; Government Code Sections 13332.17, 13400 et seq., 16304, 16304.1; State Administrative Manual Sections 8340, 10608 | | SUPERSEDES: |

TO: Agency Secretaries
Department Directors
Departmental Budget Officers
Departmental Accounting Officers
Department of Finance Budget Staff

FROM: DEPARTMENT OF FINANCE

Note: Budget Officers are requested to forward a copy of this Budget Letter (BL) to your departmental Business Services Officers.

BL 04-08 reminded departments to carefully identify the amount of encumbrances and obligations as of June 30 for the preparation of the year-end financial statements. As part of this process, departments must apply the provisions of Title 2, Division 2, Chapter 1, Article 2, Section 610 of the California Code of Regulations (CCR). CCR Section 610 provides guidelines for determining which fiscal year appropriation to charge an encumbrance and the subsequent expenditure for the purchase of goods/services. The State Administrative Manual (SAM) Section 8340 describes those documents that constitute a valid encumbrance. The accurate application of the section is essential, particularly when determining encumbrances at the end of the fiscal year. Therefore, this BL addresses CCR Section 610, including the encumbering of agreements which cover more than one fiscal year. In addition, this BL instructs departments of the timely liquidation of encumbrances.

As a reminder, encumbrances and expenditures reported on the 2003-04 year-end financial statements must be in accordance with BL 03-43 and BL 04-01.

I. Fiscal Year Appropriation to Which an Encumbrance/Expenditure is Charged

Most Budget Act support and local assistance appropriations are generally available for encumbrance and expenditure during the first fiscal year, per Section 2 of the Budget Act. This section also provides that subject to some limitations, capital outlay appropriations be available for encumbrance and expenditure for three years. Two years are then provided for encumbrance liquidation of non-federal funds, per Government Code (GC) Section 16304.1.

A. General Rule

CCR Section 610 provides that the "issue" date of an agreement for goods/services determines the fiscal year appropriation to which the encumbrance/expenditure is charged. The issue date of an agreement is the date it is "made and entered into." Any required control agency approvals are retroactive to that date. However, departments must meet the deadlines for submitting procurement documents as specified by the Department of General Services.

B. Support and Local Assistance Appropriations, Only

Encumbrances/expenditures are charged to the fiscal year in which the agreement was issued when the delivery date of the goods/services is in the same fiscal year or the delivery date is construed to mean as soon as possible. As soon as possible includes a delivery date that is:

- Not identified or specific.
- Specific but not a requested delay in delivery.
- Specified as 10 days, 30 days, or the like.

The following exceptions may apply:

- Encumbrances/expenditures are charged to the fiscal year that the goods/services are received when the purchase agreement stipulates that goods/services be delayed until requested or delayed until on or after a specific date (e.g., agreement issued in June for which the department requests equipment maintenance during the next fiscal year).
- Goods purchased and received in the months of May or June for use during the subsequent fiscal year may be paid from the appropriation for such subsequent fiscal year. Invoices covering such purchases shall be marked as follows: "Purchased in ____ F.Y. for use in ____ F.Y." Payments for such invoices may not be made until enactment of the Budget.
- Multi-year Agreements - Agreements which span more than one fiscal year may be charged (1) totally to the first year of appropriation covered by the agreement, or (2) to more than one fiscal year's appropriation, depending on the:
 - Appropriation authority – Sufficient spending appropriation authority must exist.
 - Details of the agreement

Departments will determine the budgetary plan for charging the encumbrance and subsequent expenditure when issuing a multi-year agreement. The budgeted amount will be reflected in the funding strip of the agreement. Departments have discretion as to which fiscal year appropriation to charge; however, the budgetary plan is the predominant factor in making this determination.

Departments must determine by June 30 the amount to encumber against the first fiscal year for multi-year agreements. After June 30, departments shall not encumber additional amounts to the fiscal year just ended.

II. Liquidation of Encumbrances

Most support and local assistance encumbrances remaining at year-end should be liquidated within a few months of the new fiscal year. Capital outlay encumbrances generally require more time to liquidate. Departments are instructed to closely monitor encumbrances to effect prompt delivery of requested goods or services and to ensure timely disencumbrances in instances where it is determined the goods or services will not be received or will cost less than originally estimated.

Even though the unencumbered balance is not formally reverted in the appropriation accounts of the State Controller's Office, the remaining two years prior to actual reversion are strictly for the liquidation of encumbrances accrued as of the last date the appropriation was available for encumbrance.

However, claims against a prior year appropriation will be charged to the applicable prior year when no other appropriation exists from which the claim can be paid (e.g., A utility invoice for prior year services must be paid from the appropriation year in which the services were received). This provision is without regard to the encumbrance/accrual of the claim in the year of encumbrance availability.

Additionally, the liquidation of encumbrances for multi-year agreements shall be in accordance with the budget plan when the agreement was issued. Any amounts not encumbered and not accrued to an appropriation during the period of encumbrance availability shall be paid from an appropriation that is available for encumbrance.

III. Compliance

In accordance with the Financial Integrity and State Manager's Accountability Act (GC Section 13400 et seq.), State entity heads are responsible for the establishment and maintenance of internal accounting and administrative controls. Accordingly, State entity heads must incorporate the above guidelines into operational procedures as well as conduct internal audits to ensure compliance.

The information contained in this BL will be incorporated into SAM.

Questions regarding this BL may be directed to the Department of Finance, Fiscal Systems and Consulting Unit, at (916) 324-0385, CALNET (916) 454-0385, or e-mail <mailto:fscuhotline@dof.ca.gov>.

/s/ Veronica Chung-Ng

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